

JOHN A. CHRISTENSEN AND LILA G. CHRISTENSEN (CC)

(2019) Topic Code: CO12 Capital Gain Deduction

Document Reference: 19200002

This decision has been appealed to the Iowa Supreme Court.

IN THE IOWA DISTRICT COURT FOR WINNESHIEK COUNTY

JOHN A. CHRISTENSEN, JR. and LILA G. CHRISTENSEN, Petitioners, VS. IOWA DEPARTMENT OF REVENUE, Respondent.	Case No. EQCV026248 COURT ORDER
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Hearing held August 3, 2018 on the petitioners' appeal from the decision of the respondent Iowa Department of Revenue and Finance in an income tax case. Both parties were represented by counsel of record. Dennis Larson represented the petitioners and Hristo Chaprazov represented the respondent. No evidence was presented. The hearing was reported. Counsel were granted permission to submit post-hearing briefs. Respondent's brief was filed September 11, 2018. Petitioner's brief was filed November 14, 2018. The court took the case under advisement and now makes these:

FINDINGS OF FACT

The petitioners, John A. Christensen, Jr. and Lila G. Christensen, are husband and wife and now reside in Decorah, Winneshiek County, Iowa.

The respondent, Iowa Department of Revenue is an agency of the government of the State of Iowa.

The Christensens filed a joint Iowa income tax return for calendar year 2006, reporting the sale of agricultural real estate located in Winneshiek County. Their return included a capital gain tax deduction related to the sale of the tillable land. They did not claim a capital gain deduction on the prior sale of the acreage.

The IDR audited their return and determined that they had taken an excess capital gain deduction. Additional income tax of \$6,616.00, penalty of \$1,614.30, and interest of \$296.78, totaling \$8,527.05, was assessed, based on payment by December 31, 2009. Christensens timely paid this amount to the State of Iowa, but the payment was made under protest.

A hearing on the protest was held before an administrative law judge and her Proposed Order upholding the IDR assessment was issued on January 5, 2017. This order was timely appealed to the Director of the IDR and a hearing was held before the Director. The Director's Final Order adopting

and approving the ALJ's proposed order was issued on May 25, 2017.

The Christensens then filed this petition for judicial review of the administrative action and the agency has contested the petition. The complete record of all proceedings before the agency was submitted to the district court to review on this appeal.

Lila Christensen has a brother Tom Benson. Their father owned a 96-acre farm in Winneshiek County. The elder Benson died in 1989 and Lila and Tom inherited this real estate in equal shares.

The 96 acres included a 3-acre parcel where a house and a garage were located. Lila and Tom kept the building site for their personal use, but rented out the rest of the farm consisting of tillable land, in two parcels for cash rent. Thomas Frana rented a 34.7 acre parcel and Jeffrey Miller rented 58.6 acre parcel. The building site was sold in 2005. The two parcels of tillable land were sold to the two tenants in 2006.

During the period from 1989 through 2006, neither Lila nor Tom lived on the farm. Lila lived in Loami, Illinois and Waverly Illinois during that time, and Tom lived in Des Moines and in Minnesota. Waverly, Illinois is located at least 350 miles from Winneshiek County.

Lila, John and Tom were never engaged in farming as their principal occupation. Lila was employed by a community college and later was an adoption worker. John was in the insurance business. Tom worked in the magazine publishing business.

Lila, her husband John, and her brother Tom did not farm the land during 1989 to 2006. No livestock was raised on the farm. All of the crops were planted and harvested by the two tenants, who paid cash rent to the owners and retained all of the crops harvested from the land.

The house and garage were not rented out before they were sold.

One of the tenants renting the tillable land was granted the right to use the barn and pole building when animals were kept on the premises.

The farm leases included this provision requiring the tenants to: care for the land in a good and farmlike manner and to keep the premises free from brush and burrs, thistles and noxious weeds.

The tenants decided what crops would be raised, provided all crop inputs, labor, and services. The rent charged was based upon an agreed, fixed rate per acre and was not related to production results or profitability. The landlords assumed no risk from the farming operation and had no investment in the crops.

The Christensens testified that that their oral agreement with Tom was that Tom would do the work needed to maintain the house and building site and they would do the work needed to manage the rental of the tillable land.

John testified that he and Lila prepared the cash farm leases following negotiation with the tenants handled all matters requiring contact with the tenants, removed brush and trees as needed, and repaired fences and buildings when needed. Tom wrote all the checks to pay farm related bills, until 1999 when John retired and the Christensens took over that chore.

The Christensens did not own any other farmland. This was the only farmland they leased out as landlords.

CONCLUSIONS OF LAW

The court has jurisdiction of the parties and the subject matter of this case as provided by Chapter 17A and Division II of Chapter 422 of the Code of Iowa.

In an appeal from the decision of an administrative agency, the district court may reverse, modify or grant other appropriate relief if the agency's decision is not supported by substantial evidence in the record. See Section 17A.19[8][f], Code of Iowa.

Evidence is substantial if reasonable minds would find it sufficient to reach a conclusion. See *Quaker Oats v. Ciba*, 552 N.W.2d 145 (Iowa 1996) and *City of Davenport v. Public Employment Relations Board*, 264 N.W.2d 307 (Iowa 1978).

The protesting taxpayer bears the burden of showing that the tax assessment was erroneous. See Section 422.60[6][c].

Section 422.721[a] of the Code of Iowa gives taxpayers a deduction for net capital gain income from taxable income from the sale of certain business property, including farm property, if the taxpayer materially participates in the business for at least 10 years.

The sole issue in this case is whether the taxpayers materially participated in the business. The IDR has adopted administrative rules to assist in determining whether a taxpayer can meet the material participation test. See IAC 40.38[2].

IAC 40.38[1] sets out 7 tests to determine material participation. Test 4 includes the Cash farm leases and states:

“A farmer who rents farmland on a cash basis will not generally be considered to be materially participating in the farming activity. The burden is on the landlord to show there was material participation in the cash-rent farm activity.”

The agency determined that the type, duration, and significance of the participation provided by this taxpayer in the rental activities of this property fell far short of those required to establish material qualification and obtain the capital gain deduction.

Based upon its review of the record, this court concludes that the agency decision was supported by substantial evidence in the record.

COURT ORDER

It is ORDERED that:

The appeal is denied and the decision of the agency is affirmed.

Costs on appeal are assessed to petitioners.

The clerk shall furnish copies of this Order to counsel of record.

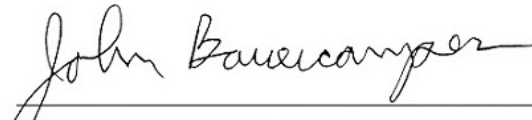


State of Iowa Courts

Type: OTHER ORDER

Case Number	Case Title
EQCV026248	JOHN & LILA CHRISTENSEN VS IOWA DEPT OF REVENUE

So Ordered



John J. Bauercamper, District Court Judge,
First Judicial District of Iowa